An Analysis of Macro Mechanisms in the Development of Chinese Outward Foreign Direct Investment

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Introduction

Developed countries boast a large number of transnational corporations and are the biggest winners in the process of economic globalization. We now consider how China develops its own transnational corporations to take part in international competition for a share of global markets and global resources.

China has more than 30 years’ experience in the growth of its transnational corporations, which has been characterized by rapid economic development. From 2007 to 2015, China’s outward foreign direct investment (OFDI) increased by 24 percent per year, from US$26.5 billion in 2007 to US$145.7 billion in 2015 (Table 1).

However, behind the high-speed development in the cross-national operations of Chinese enterprises, there exist problems such as their small scale, inefficient operational levels, small-scale investments, and poor profitability, which are in contrast with the fast-growing Chinese economy. China’s performance in OFDI is unsatisfactory, and an important reason why is that China’s OFDI macroeconomic mechanism is not perfect. Under this economic system, however, whether an enterprise can realize OFDI can be one factor of effective management in operations overseas.

Consequently, besides forming and strengthening its competitive advantages to enable enterprises to meet the...
requirements and competencies of cross-national operations, China should also establish and form a mechanism that is beneficial to the rapid growth of Chinese transnational corporations. This article emphasizes the external requirements of and environments for the development of OFDI, which amounts to analyzing the growth mechanism of Chinese transnational corporations. It is obvious that current mainstream theory regarding transnational corporations is based on the foreign direct investment (FDI) behaviour of corporations under market economy systems. Therefore, it cannot offer a full explanation for the OFDI behaviour of China’s state enterprises, which enjoy government initiatives and strong capabilities to adjust to macro policies and related mechanisms. The present article fills this gap. This article discusses this problem, provides suggestions for improving the OFDI macro policy mechanism for promoting Chinese OFDI, and improves on existing FDI theories. This article deals with several basic aspects of the OFDI macro mechanism that affect the smooth progress of China’s OFDI. Similar developing countries and economies will face the same problems, so this research has a very realistic significance.

Many previous studies have focused on the trends and pattern of inward FDI in China and other developing countries. Sauvant and Mallampally (2015) and Sauvant (2015) presented an overview of the benefits of inward FDI for the developing countries and the policies pursued by host economies to promote inward FDI. Kishor and Singh (2015) examined the factors that affect inward FDI in BRICS economies. This differs from those studies by focusing on outward FDI in developing economies.

As shown in Figure 1, the six main impact mechanisms for OFDI of Chinese enterprises are the policy, legal, monetary support, service support, tax, and insurance mechanisms. The first two mechanisms affect whether an enterprise can successfully undertake OFDI, the last two mechanisms affect the enterprise’s operation overseas after making an OFDI, and the service support mechanism affects both OFDI and the enterprise’s operations overseas. These two aspects, OFDI and operations overseas, are the two stages of growth and survival for multinational companies. This article explores the relationship between the macro mechanism of OFDI and the growth and development of Chinese multinational corporations and the relationship among the various macro mechanisms.

### Literature Review

China’s economy is a market economy in transition. An important feature of this type of economy is the strength of economic interventions by the government, which take place when the government strives to implement its national strategies. Such interventions are carried out via relevant macro adjustment mechanisms to guide or restrict company behaviours. This situation will persist, so one of the determinants of FDI by Chinese companies is that although the company is the sole investor, it has to go through various stages stipulated by the government to get final approval to conduct OFDI, in addition to its own ability and motivation. While the company goes through these stages, it may be restricted in conducting OFDI on the basis of relevant policies and regulations, or it may miss the best investment opportunities because of delays in approval caused by bureaucracy. However, companies that otherwise would not engage in OFDI may choose to do so in a timely manner thanks to the leverage provided by such policies and regulations. This is what is termed the functionality of macro mechanisms in OFDI by Chinese companies.

The classic theory of FDI is mainly derived from various aspects of the growth of multinational companies in developed countries. These aspects include the capability of enterprises (e.g., the dominance of a monopolistic position; Hymer 1976 [1960]), the conditions for FDI by enterprises (e.g., the eclectic paradigm of international production; Dunning 1988), and the internal market formed by the enterprise to avoid risks in the external market so as to maintain its advantages (e.g., internalization theory; Buckley and Casson 1976), as well as enterprises’ motivation for FDI (e.g., resource-seeking FDI, market-seeking FDI, efficiency-seeking FDI, strategic asset-seeking FDI; Dunning 1988).

The theory of FDI that is most relevant for this paper is Dunning’s Eclectic Theory of International Production or the OLI paradigm (Dunning 1988). According to that theory, for a direct investment to be beneficial, there must be ownership advantage (O), location advantage (L), and an international advantage (I).

### Table 1: Scale of China’s Outward Foreign Direct Investment

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<tr>
<td>FDI flow ($US billion)</td>
<td>26.5</td>
<td>55.9</td>
<td>56.5</td>
<td>68.8</td>
<td>74.7</td>
<td>87.8</td>
<td>107.8</td>
<td>123.1</td>
<td>145.7</td>
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<tr>
<td>Growth rate (%)</td>
<td>25.3</td>
<td>110.9</td>
<td>1.1</td>
<td>21.7</td>
<td>8.5</td>
<td>17.6</td>
<td>22.8</td>
<td>14.2</td>
<td>18.3</td>
</tr>
<tr>
<td>FDI stock ($US billion)</td>
<td>117.9</td>
<td>184.0</td>
<td>245.8</td>
<td>317.2</td>
<td>424.8</td>
<td>531.9</td>
<td>660.5</td>
<td>882.6</td>
<td>1,097.9</td>
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Note: FDI = foreign direct investment
Sources: Authors’ tabulation based on the data from the National Bureau of Statistics of China

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**Authors' note:**

1. **Table 1:** Scale of China’s Outward Foreign Direct Investment

2. **Note:** FDI = foreign direct investment

3. **Sources:** Authors’ tabulation based on the data from the National Bureau of Statistics of China

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**References:**


doi:10.3138/cpp.2016-076

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**Note:**

This research examines the factors that affect OFDI, which are crucial for the growth and development of Chinese multinational corporations. The study focuses on the macro mechanisms that influence OFDI, providing insights into the policy implications for promoting OFDI in China.
Figure 1: Mechanisms of development of outward foreign direct investment in China
Note: FDI = foreign direct investment.
Source: This figure is drawn by the authors based on the information from Sauvant and Mallampally (2015), Sauvant (2015), and Kishor and Singh (2015), etc.
These theories offer explanations for enterprises’ FDI practice in countries with a market economy, where governments pursue liberal economic policies and do not or rarely interfere with the operations of enterprises. Thus, in a typical market-economy country, macro mechanisms affecting enterprise FDI activities play a limited role, whereas the opposite is true in China. This poses a challenge to the explanatory power of existing FDI theory; therefore, the theory needs improvement and revision to adapt it to the Chinese context.

OFDI and overseas operations by Chinese enterprises are determined not only by the capability and conditions of the enterprise concerned, but also broadly by the mechanisms of the government’s macroeconomic policies. China’s OFDI lacks structural balances in terms of principal investor, investment location, and choice of industry; there are also deficiencies in OFDI management and promotion. China must strive to promote the marketization process for financial markets, interest rates, and exchange rates to gradually eliminate administrative monopoly, improve administrative efficiency, and promote the healthy development of China’s FDI (Gao and Kang 2011).

Overall, the quality of Chinese OFDI is still low, and there is therefore a need to increase investment in countries with high-quality systems so as to promote continuous improvement in the quality of domestic institutions and regimes. This can be achieved via impacts and integration between the domestic and overseas systems to gain spillover and reverse effects at the system level. Rao and Zhu (2015) find that the differences in the quality of institutions between China and the host country have a significant impact on China’s OFDI. An examination of the Chinese OFDI system shows that Chinese OFDI tends to go for a host country that is considered better than China in terms of rule of law and corruption control. When it comes to government efficiency, the bias is dichotomous; on the one hand, among countries whose governments are more efficient than China’s, Chinese OFDI is biased toward the richer ones; on the other hand, among countries whose governments are less efficient than China’s, Chinese OFDI tends to favour the poorer ones.

Sauvant and Chen (2014) conclude that the short-term challenge facing the Chinese government’s OFDI policy is to eliminate the concerns of the host country and guide Chinese enterprises through OFDI to help the host country’s construction and development. The medium-term challenge is to develop and implement the right financial incentives and financial subsidy mechanisms to promote enterprises’ OFDI; the long-term challenge is to build a multilateral framework for investment to become a real maker of rules.

Sauvant (2013) analyzes the scale and structure of China’s OFDI and the driving factors of China’s OFDI growth. A macroeconomic analysis of the influencing factors and causes of Chinese OFDI concludes that the contributions of macroeconomic, monetary policy, and fiscal policy factors to Chinese OFDI growth were 49.16 percent, 25.04 percent, and 8.18 percent, respectively. This shows that the domestic economic situation and conditions have a direct impact on OFDI, and the impact of the monetary policy mechanism is stronger than that of the fiscal policy mechanism.

Wang (2016) constructs the game theoretic model between the OFDI of Chinese enterprises and the government support policy and concludes that the OFDI of enterprises and government support is positively correlated; government support is not only good for business but also advantageous to the government itself. Government support policies include preferential loans, tax and other financial support, and industry information, laws and regulations, and risk assessment services support.

Some scholars have noted an improvement in China’s FDI macro policies and that China’s government has planned to reduce its role in commercial decision making and seems more comfortable with allowing both nationalized and private businesses to pursue growth on the basis of maximizing shareholder value rather than enhancing national security (Dobson 2014).

A variety of macro mechanisms affect enterprise OFDI. The basic forms of macro mechanisms are policies, regulations, and regimes. Since 2009, the Yearbook of International Investment Law and Policy, published by Oxford University Press, has contained expert analyses of the past year’s developments in FDI, international investment agreements, core of disputes, and laws and policies regarding FDI. Clearly, the macro mechanism of international direct investment necessarily affects Chinese enterprises’ FDI and whether they achieve operating efficiencies of international investment afterward. The present article summarizes six macro mechanisms; among them, the policy, legal, monetary support, and service support mechanisms are mainly to promote or regulate enterprises’ OFDI; the tax, insurance, and service support mechanisms serve to help and improve the overseas operations of enterprises that have already achieved OFDI. However, each of these mechanisms exerts influences at times and with strengths that cannot specifically be determined, and there is also no particular order in which they exert their influences.

Analysis of the Mechanisms Governing China’s Outward Foreign Direct Investment

This section analyzes the six main mechanisms affecting Chinese OFDI and its operations overseas. It begins with
one of the key factors essential to the analysis of OFDI behaviour of Chinese corporations, the role of state foreign investment policies in determining corporations’ off-shore investment behaviour.

Policy Mechanism

Governmental policies play a very direct and pivotal role in the development of OFDI. Under current governmental policies, more systematic theories regarding the development of transnational corporations have not been developed. However, any country’s policies aimed at boosting the development of OFDI are a part of that country’s overall strategic considerations. In a market economy, the cross-national operations of the enterprise are mainly corporate behaviours with minimal influences from governmental policies. This is the reason why there are few theories relating policies to the development of OFDI. In reality, once the government realizes the overall long-term strategic significance of transnational corporations, the promotional and mechanistic role of policies will emerge accordingly. However, the present policies undertaken by the Chinese government are unfavourable for the development of OFDI and therefore require modification.

Foreign Exchange Administration

The purpose of a country’s foreign exchange administration is to maintain its international balance of payment equilibrium, an orderly exchange rate arrangement, and financial stability. To some degree, strict foreign exchange administration is the outcome of economic underdevelopment and inadequate opening up. When there is an insufficient ability to earn foreign exchange, along with a disconnect between domestic and foreign price systems and unsteady macro financial systems, it is necessary to establish and strengthen the system of foreign exchange administration. At present, a significant conflict exists between the development of offshore investments and the foreign exchange administration in China.

The functions of foreign exchange administration departments in China in relation to offshore investments mainly include the following: first, evaluating the risks and sources of foreign exchange after the offshore investment project is put forward; second, administering foreign exchange after the offshore investment project is approved; third, financing administration of the offshore investment project; and finally, administering deposits remitted by offshore investors.

The current foreign exchange administration discourages enterprises from making offshore investments, which is reflected in the following aspects. First, the overstrict foreign exchange control affects offshore investment. According to the regulations, when enterprises make offshore investments, those who have foreign exchanges initially make investments with their own foreign exchange; those who lack a foreign exchange can make FDIs with a loan. Enterprises are also encouraged to make real investments or are allowed to export without settlement exchange. However, the overwhelming majority of Chinese enterprises have a limited foreign exchange, with insufficient competences and conditions to raise loans for offshore investments and great difficulty in real investments. As for investment by product export without settlement exchange, it is to some extent a good way to solve the funding problem for offshore investments, but it is still restricted by the enterprises’ sales capability. In addition, products exported will not turn into investment capital until they are sold out. Consequently, opportunities for investments in many projects will be lost because the foreign exchange funds cannot be acquired in time. Obviously, these regulations are unfavourable for enterprises looking to expand the scale of their offshore investments and to operate efficiently. Moreover, the current regulations, which also prohibit enterprises from purchasing foreign exchange for investment in the ownership of offshore shares, are more likely to cause enterprises to lose valuable opportunities with respect to holding shares or cooperative projects.

Second, the system of deposits remitted from profits is adverse to enterprises’ capital turnover. According to the rules of offshore investments, 5 percent of the total amount of foreign exchange funds remitted will be kept as a deposit; profits from offshore investments and other foreign exchange incomes should be transferred back home 6 months after the end of the local fiscal year. As an important part of China’s foreign exchange administration, the system of deposits remitted from profits is to guide enterprises to remit their earnings from offshore investments to home and to improve payment balance conditions. However, the system results in an overstocking of enterprises’ funds, causing enterprises to have trouble turning over funds and influencing their normal operations. For most enterprises that have just begun investing from scratch, it is hard to make a profit. The overstocked deposits will undoubtedly increase the burden on the enterprise. Moreover, if the reinvestments made after profits are remitted back, they will go through complicated procedures.

Third, the restriction of international business loans causes enterprises to be unable to take full advantage of the international capital market to conduct financing. Making good use of the international capital market to conduct overseas financing is one method adopted by Chinese enterprises lacking enough capital, and it is also a typical way for transnational corporations to operate. However, the foreign exchange control authorities in China place the international business loans used by domestic enterprises for offshore investments in the category of foreign loan administration. A strict examination
and approval system is implemented, and domestic enterprises are obstructed from making good use of the outer capital market. It is quite unfavourable for domestic enterprises to use international business loans for offshore investments. In reality, by taking advantage of the international capital market, enterprises can often acquire more advantageous financing terms, achieve lower financing costs, and obtain important information related to projects, thus enhancing their international competitive advantages.

In 2003, the Bureau of National Foreign Exchange Administration approved 10 provinces as experimental provinces for the reform of foreign exchange administration. These experimental provinces possess a foreign exchange quota from US$50 million to US$200 million. Within the quota, projects below $3 million foreign exchange are examined and approved by the local branch of the foreign exchange administration. The problem of enterprises purchasing foreign exchange for investments is one part of such an experiment. For instance, the Beijing foreign exchange administration department acquired a quota of US$200 million foreign exchange for domestic enterprises for offshore investments, which helped solve Shougang’s problem of obtaining foreign exchange for the ownership of shares. Because Shougang is one of China’s largest state-owned enterprises, it quickly got the government’s support, which tends to support large, state-owned enterprises. Faced with the same situation, private enterprises will not get this support.

The problem regarding profit remitted is also one main part of such an experiment. Domestic investors can decide independently whether to remit profits back from offshore investments or to change profits into local capital to expand the investment scale. This can be realized by reporting to foreign exchange administration departments for records. A series of reforms in the foreign exchange administration, an important mechanism for growth and promotion, has stimulated the development of Chinese enterprises’ cross-national operations and the growth of Chinese transnational corporations, but it needs time to extend countrywide.

In December 2014, the central government and the State Administration of Foreign Exchange made it clear that the administration of foreign currencies for offshore investment will change from corporations having to register with relevant governing bodies fulfilling requirements at the bank when remitting foreign currencies. This stipulation has greatly simplified the approval process.

Administrative Examination and Approval
The formation and real situations of China’s administrative examination and approval of offshore investments are influenced by historical as well as practical factors. First, China’s overall economic strength is not strong enough to reach the mature stage for FDI. Second, at present, China does not qualify for the conditions of capital items convertibility. Although the level of China’s exchange reserve and the balance of international payment position are no longer the main factors restricting direct offshore investment, capital account convertibility should be carried out step by step. Otherwise, great risks will be incurred. Finally, the dual-economy characteristics of China’s economy are rather obvious; industrialization is still underway, and the domestic economy requires a lot of funds. The establishment of a system of administrative examination of and approval for offshore investments is the outcome of these factors. This system lags behind the development of new situations: (a) The excessive administrative levels of examination and approval cause missed opportunities and increased costs; (b) examination and approval are overly detailed and repetitive, and the system of examination and approval is opaque, which leads to inefficient examination and approval; and (c) some vulnerability exists because difficult enterprises tend to acquire the relevant preferential policies.

The current system for approval of overseas investment and management became effective on 1 August 2008. It has established the transition of the management of overseas investment from the current approval system to a less stringent check-up system. The roles of the National Development and Reform Commission and the Department of Commerce were also made clear, with the commission being responsible for checking on overseas investment projects and the Department of Commerce being responsible for checking on corporations undertaking an investment project. It has also established the transition of the management of foreign exchange from the compulsory exchange settlement to a voluntary exchange settlement. On 16 March 2009, the current system was revised to further define the check-up boundaries. Compared with the check-up boundaries stipulated in 2008, those issued in 2009 are more flexible and accommodating.

Home country regulations and the hierarchical systems that operate in relation to OFDI in China have also served at times to militate against Chinese FDI overseas, especially in developed countries. This is especially the case in relation to acquisitions, in which the freedom to respond quickly in a bidding scenario can be critical to a successful outcome. However, China’s regulatory framework dealing with OFDI is undergoing significant change as a result of the reforms signalled by the government, with only deals valued at more than US$1 billion now requiring a full review by the National Development and Reform Commission as compared to the previous threshold of US$100 million, thus largely removing one
stage of the approval process for such investments. Nonetheless, there is still some way to go in terms of simplifying the system regulating OFDI (Brennan 2015).

The administrative examination and approval is necessary, but more important is whether it is efficient and favourable for enterprises to increase their competitive advantages in offshore operations.

**Assets Administration**

Assets administration is one part of the policy mechanism for the growth of Chinese transnational corporations. Its basic logic is that enterprises that go global become transnational corporations and, if they want to expand effectively, offshore property should be well administered and kept intact. Transnational corporations’ administration of offshore assets has been a core issue in their offshore growth. The effective management of offshore assets is associated with a series of policies, such as the functions of government departments, the company’s structure, the parent company’s control over its subsidiaries, and the exterior supervision of the investment corpus. Furthermore, when any enterprise, no matter what its character is, becomes a transnational corporation and turns its offshore investments into offshore assets, these assets become national assets according to the national principle in national economic accounting, which is different from the attribute demarcation of assets in its domestic operations. Therefore, the country claims responsibility for keeping offshore assets intact and avoiding the risks, such as escapes and loss. With respect to asset administration, the country’s responsibilities lie in supervision over offshore assets in different forms and to different degrees.

At present, large enterprises dominate in undertaking offshore investments. In spite of the different ownerships of these large enterprises, the most competitive and the largest number among them are state-owned enterprises. Therefore, the administration of offshore state-owned assets is a main consideration. It should be realized that no matter what the character of enterprises making offshore investment is, their offshore assets are national assets and are one form of national wealth. Because enterprises keep their offshore assets intact and promote a rise in value out of their own interests, requirements, and motives, the country should regard them as overall national interests and claim responsibility for guaranteeing their safety and supervision in some form.

So far the government has not clarified its position on the monitoring and management of off-shore state assets. Because the scale of overseas investment by Chinese corporations is rapidly expanding, any oversight of monitoring and managing such assets can result in the risk of their loss.

**Legal Mechanism**

Laws and regulations are necessary to regulate all relationships between corporations. They can restrict the relevant behaviours of corporations and protect their interests. If enterprises in China hope to grow into transnational corporations, their legal status and the form and behaviour patterns acknowledged by laws and regulations need to be affirmed. They need to get the most authoritative safeguard, which is the legal mechanism that promotes the growth of Chinese transnational corporations. In this respect, there are two problems.

First, the legal system regarding Chinese enterprises’ offshore investments has not yet been formed, as there are no written legal documents that take into account offshore investments by Chinese enterprises. In this respect, the system of laws and regulations has yet to be developed. Some are outdated, and the measures and the scope of adjustment have not been suitable for the development of Chinese enterprises’ offshore investments. For example, although a series of present legislative files regarding offshore investments are directed at offshore investment by state-owned enterprises, in the practice of Chinese offshore investments, private enterprises need direct offshore investments and are doing so now. Until now, China has not had a single fundamental law regarding the modulation of offshore investments and has also lacked the corresponding legal system, which causes the absence of legal evidence and macro guidance in practice. All of these factors bring about a certain degree of blindness in China’s offshore investments and unreasonable investment locations and industrial choices. Some drawbacks have been occurring, and national interests have been harmed in offshore investments, which causes loss of national assets and sometimes subjects corporations that observe laws to missing out on opportunities and legal advice.

Second, the protection mechanism from international laws for bilateral or multilateral investments has yet to be formed. Offshore investments involve two or more countries and are typically international affairs. The law of home countries cannot protect the benefits of their enterprises making offshore investments. Internationally, along with the larger and larger sum of cross-national funds and involvement of more and more countries, a legal system for international investments and relevant regulations will be established and be carried out accordingly. Normally, to attract and administrate foreign capital, the host country will formulate specific laws and regulations. Similarly, the home country will adopt policies to encourage and protect its domestic enterprises in their offshore investments. However, given the obvious differences in socioeconomic systems and technological levels between nations, the legislation of a
single country cannot play a full role in protecting the safety and interests of investors. When it comes to some major problems regarding conflicts of interest, such as the treatment of foreign capital, nationalization, the settlement of investment disputes, and so forth, domestic laws cannot solve them thoroughly. It is necessary to appeal to international laws and establish a double-lateral or multilateral cooperative mechanism to promote economic and technological cooperation based on mutual interests between nations, to maintain a favourable investment environment, and to protect foreign investors internationally.

Given that China has established domestic legal systems regarding offshore investments and takes part in and advantage of international bilateral or multilateral legal systems to protect investments, they will be an important mechanism to protect the interests of Chinese offshore investors and to promote the growth of Chinese transnational corporations. China should stipulate normative OFDI behaviour. This can be done at the state level to establish basic legislations, at the local level to develop functional specifications for OFDI, and at the international level to formulate bilateral or multilateral agreements. These will result in a complete as well as a healthy legal system for OFDI.

**Monetary Support Mechanism**

The prerequisite for an enterprise to become a transnational corporation to affect FDI is to first possess funds. Most of the time, it is hard for enterprises to solely depend on their own funds to provide the investment funds involved in projects. Even when they have made investments, it is hard for them to conduct the normal turnovers and operations. The most common solution is to acquire financial support or to conduct capital operations in capital markets. The degree of financial support, which is embodied by domestic financial support policies and given to enterprises’ offshore investments, reflects whether governmental policies are encouraging or restrictive.

In China, the monetary support policy for offshore investments is mainly in the form of guidance and regulation (e.g., MOFCOM 2002). The main objects are the enterprises that conduct assembly and process materials. The main contents include allowing domestic banks to provide financing to offshore investments that meet the requirements; favourable loan interests; precedent provision of export loan; and direct financial support.

In China, the financial support mechanism for offshore investment is primitive, and the support is not strong enough. China is far from forming financial support systems and lags behind in the development of OFDI, which is manifested as discussed in the following paragraphs.

First, the scope of the monetary support mechanism is limited, with inappropriate guidance. Two aspects are included. The first is that a favourable financial support policy is directed at the business of processing materials and conducting assembly with local inputs. The second is that favourable financial policies have obvious limitations on ownership of enterprises.

The financial support policy should first abandon the discrimination in ownership and regulations that restricts financial support projects to the business of processing materials and conducting assembly of products overseas.

Second, the monetary support has little strength. The benefits with respect to interest and loans are of little substantial significance, that is, there is no strong support. In practice, loans provided by import–export banks are limited and have a single form, which is a substantial difference from the monetary strength and forms of loans from many other countries.

Third, monetary support mechanisms have low operational efficiency and high costs, along with insufficient transparency of policies. With strict standards of examination and approval, there are multiple same-level government departments and complicated and repetitive procedures. Therefore, the present financial support is inefficient.

As a crucial part of the support mechanism, monetary support is expected to enable enterprises to achieve overseas expansion to become transnational corporations. At a governmental level, significant improvements should be made in the following aspects: expansion of the scope of monetary support policies, increase in support strength, and increase in efficiency and transparency. These will lead to an important promotion mechanism for the growth of Chinese transnational corporations.

While policy-supported financial institutions did play a substantial role in promoting foreign investment, the current practice indicates that support to large projects is quite sufficient, whereas that to medium and small projects is inadequate.

**Tax Mechanism**

Given a monetary support mechanism that determines whether enterprises will be able to take the first step during offshore investments, the tax support mechanism is introduced as a promotion mechanism for effective operation of the enterprises that have already made offshore investments. Its role is to reduce burden, financially guarantee and support enterprises in operating normally, and expand their scale and increase their competitive advantages.

Offering monetary support and preferential tax measures is the customary practice of many countries and economies to encourage their enterprises to develop offshore investments and to support the growth of their transnational corporations.
In China, such policies have so far been limited to providing financial support and preferential tax measures to businesses that process materials and conduct assembly with overseas inputs. After the first year in which such enterprises show a profit, they are allowed to supplement their capital funds with the succeeding five years’ profits with the purpose of expanding the scale of their production and are not obligated to submit these profits to the government. As physical investments, enterprises’ export equipment, raw materials, and scattered parts enjoy export drawback. Among them, the duty drawback of second-hand equipment is calculated according to the balance after depreciation, whereas the duty drawback of new equipment and raw materials is calculated according to the sum of income taxes listed in the specific invoices for value-added tax.

With respect to offshore investments and the promotion of OFDI development, China’s tax support mechanism has significant problems in terms of narrow scope, non-sufficient support strength, and lagging economic development.

**Insurance Mechanism**

Compared with domestic investments, offshore investments tend to face more risks, such as business risks and political risks. The occurrence of these risks will bring different degrees of loss to offshore investors’ operations. Some of them involve life-or-death situations and seriously affect investors’ operations. The effective way to manage and prevent risks is insurance, but many risks related to offshore investments are not covered by insurance companies, which require the country to establish a corresponding offshore investment insurance mechanism to protect the interests of offshore investors and to promote the development of OFDI.

Along with the growth of China’s economy, enterprises will inevitably strengthen their competitive advantages, grow into transnational corporations, and encourage more foreign investments.

**Service Support Mechanism**

The service support mechanism for the growth of China’s transnational corporations incorporates a series of elements and systems that increase operational efficiency, survival capability, and competitive advantages and improve their development conditions. The service support for enterprises’ offshore investment has wide content and form, is a basic requirement for the development of transnational corporations, and is the promotion mechanism for a nurturing environment. Service support mechanisms include (a) information assistance, (b) technological support of investments and personnel training, (c) cooperation between governments, and (d) intermediary organizations. The current guideline for the service support clearly stipulated the types of industry in which investment is encouraged and those in which investment is prohibited. For industries in which investment is encouraged, the state will provide relevant policy supports in terms of macro control, multilateral and bilateral economic and trade policy, foreign affairs, finance, taxation, foreign exchange, customs, resources, information, credit, and insurance, as well as bilateral and multilateral cooperation and foreign affairs. As of January 2012, China and other economic entities had signed 132 bilateral investment treaties, which provide, to some extent, a means of protection for corporations undertaking normal overseas operations.

**Conclusion**

Along with the deepening of reforms, opening up, and fast economic development in China, more and more Chinese enterprises, in the process of economic globalization, make FDI, conduct cross-national operations, and grow into transnational corporations. This trend is inevitable. The growth of Chinese transnational corporations is of important and strategic significance to China. It is a necessary step for China to capture the international market more extensively, to utilize and allocate global resources, and to upgrade the domestic industry structure. In the process, China will be able to acquire tremendous economic benefits and improve its economic status and influence on the international stage. If Chinese enterprises hope to become transnational corporations, they need to improve their competitive advantages and exert their ownership-specific advantages.

The external environments that nurture the growth of Chinese transnational enterprises also play an important role and are the relevant mechanisms influencing their growth. However, the main aspects of these mechanisms are apparently adverse to the growth of Chinese transnational enterprises and do not exert their roles of facilitation. For example, the foreign exchange administration maintains a strict administration mode, which means restricting the use of foreign exchange by enterprises, restricting enterprises from spending their own funds to purchase foreign exchange and expanding their shares, and carrying out the system of deposits remitted from profits of FDI.

As far as the legal mechanism is concerned, China should accelerate fundamental legislation on transnational corporations, specify the status of and necessity for transnational corporations, standardize corporations’ behaviours and safeguard their interests, and thus promote their healthy and fast development. As to China’s current administrative examination and approval, there exist such problems as excessive links, repetition, inefficiency, and insufficient transparency, which lead to increased costs and lost business opportunities. At present,
the Chinese government intends to change the practice of registration with relevant bodies for foreign exchange for overseas investment to fulfill only the required procedures when remitting foreign currencies at the bank. This will greatly simplify the approval process.

In terms of administration of assets, assets financed by Chinese FDI, including state-owned and private investment assets, should be regarded as national assets and administered scientifically. Meanwhile, relevant government administration departments should conduct the necessary supervision to keep them intact, promote a rise in value, and avoid such risks as escape and losses. With respect to monetary support, besides its little strength, what is restricted are investment and production projects that process materials and conduct assembly of goods overseas and state-owned enterprises, which apparently ignores the investment in market seeking, resource seeking, and strategic assets seeking, as well as support to the offshore investments of private enterprises.

In terms of tax support, China should sign more relevant tax agreements to protect the interests of Chinese offshore investors, reduce their burden, promote effective operations, and expand their scale. As far as insurance mechanisms are concerned, the management of offshore enterprises’ non-business risk—which business insurance organizations are unwilling to insure—should be established and strengthened. Also, international cooperation on insurance should be strengthened, and relevant insurance agreements should be signed quickly to safeguard the safety of Chinese offshore operations.

As to information support, Chinese enterprises have not enjoyed premium and complete services, which influence their ability to go global smoothly. In this aspect, the following are to blame: insufficient information support and technological assistance; cooperation between governments that cannot better meet the requirements of enterprises operating in host countries; insufficient intermediary services; and low quality of intermediary services. In general, the objective mechanisms to promote the growth of Chinese transnational corporations still require improvement and development, and great effort should be made. These factors are of great significance to the growth of Chinese transnational corporations.

The macro mechanisms of OFDI, some mandatory, others regulated, will gradually change. For example, a project approval policy will be implemented, but with the further opening up and national macro strategy implementation, the degree of control and scope will be weakened and reduced. China has large-scale foreign exchange reserves and sustained growth of its economy, but it also faces the risk of devaluation. Chinese enterprise OFDI is an effective release channel to alleviate the pressure; therefore, foreign exchange control policies will be further relaxed. In recent years, the Chinese financial situation has improved significantly, and the growth rate of local finance in many provinces is faster than the local GDP growth rate, so tax incentives and financial support of special macro policies will also emerge. We believe that project approval will be implemented, but it will not only be project based but also take into account the industry to which the project belongs, the credibility of the distinction between companies, and the use of sub approval to encourage enterprises to OFDI. Foreign exchange management can be further relaxed. On the one hand, it can guarantee the enterprise will get foreign exchange support. On the other hand, it can also clear the scale of the enterprise’s own foreign exchange. Fiscal and tax support can increase strength. Fiscal and tax support are mainly used to support the strategic significance of important projects and to encourage enterprises to develop overseas markets and industry layout.

The present article holds the view that the reforms in China’s macro policy mechanisms are of great significance in nurturing China’s transnational corporations. On one hand, the reforms promote Chinese corporations’ OFDI; on the other hand, they protect Chinese transnational corporations engaging in overseas operations and their off-shore capital. The result of the current research implies that Dunning’s Eclectic Theory of International Production, or OLI paradigm (Dunning 1988) ought to be extended to include a policy mechanism, namely becoming the OLIS paradigm, where S = system or policy mechanism. The extended paradigm will have a stronger explanatory power and a wider range of adaptability if S is added to it.

References


